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When Economists “Tell Histories”: the Truncated Story of Central Banks’ Cooperation over the Bimetallic Period

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Abstract: »Wenn Wirtschaftswissenschaftler „Geschichten“ erzählen: die verkürzte Geschichte der Kooperation der Zentralbanken über die bimetallische Periode«. In this article, we assess the meaning of the controversies about the French and British central banks’ solidarity over the bimetallic period (1850-1870). Our purpose is to highlight how historical case studies can become the instrument of a distorted economic view. In the main stream literature, the argument of the discount rates correlation is turned into rivalry between the two issuing institutions. This view omits the reading of Bimetallism as a coordinated discount rate policy of the French and British central banks and supports bimetalism as a self-equilibrating system.

Keywords: bimetalism, central bank cooperation, cliometrics.

Introduction

In contrast with conventional wisdom on Bimetallism, Parent (2006) and Diebolt and Parent (2008 and forthcoming) found cliometric evidence that French and British central banks did co-operate making Bimetallism a very early regulated monetary regime. This thesis calls into question the academic view according to which the *Banque de France* was mainly a domestic issuing institution in the mid-19th century as well as the scepticism around the idea of central bank co-operation over the 19th century (Flandreau, 1997).

We consider that most of the existing arguments corroborating the thesis of the non-cooperation that can be found in the literature on the double standard are weak and fragile. Above all, they carry a very classical view of the distinction between Economics and History, limiting the added value of History to the field of the historical context (as opposed to “a-historical” cliometrics). The purpose of this article is to underline the dangers of the supposedly neutral interpretation of historical features when it is actually a pretext for a specific economic discourse. This raises the issue of History as the instrument of historical economics.

In this article, we shall recall the controversies about the French and British central banks’ solidarity during the bimetallic period. Our purpose is to high-

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light how this “story” was truncated in order to corroborate a specific economic view. The two main channels of the story of Central banks “solidarity” considered as war are:

- first, the thesis of non cooperation which relies on three episodes only over the entire bimetallic period;
- second, the argument of the discount rates correlation turned into rivalry between the two issuing institutions.

1. The controversy around central banks cooperation

To date precisely the beginning of the cooperation between international central banks is an important issue in recent economic literature. We review below the pros and the cons. Flandreau (1997) argued that “central bank cooperation was probably not decisive in the operation of the gold standard” (p. 735)... “Co-operation had been exceptional, never reciprocal, and always failed to institutionalize... what has been interpreted as cooperation was the product of the selfish interest of central banks; they helped each other only when this provided a direct benefit to them, instead of mutually adjusting towards some cooperative equilibrium as hypothesized by the cooperation view” (p. 737)... “It should be clear that central bank cooperation was definitely not the predominant pattern in the pre-1914 period. Hence, one must reject the view that central bank cooperation was an essential ingredient of exchange rate stability” (p. 760). This echoed Viner’s views of the mid-19th century: “Co-operation between central banks was during this period exceptional rather than an established policy. On the contrary, it appears that ordinarily the central banks either paid little attention during this period to what was going on in other money markets, or else engaged in competitive increases of their discount rates and in raids on each other’s reserves at a time of actual or anticipated credit stringency” (Viner, 1937, pp. 274-275).

This approach is subject to debate. In the introduction to *Golden fetters*, Eichengreen (1992) underlined that central bank co-operation had been the key to the exchange rate stability of the pre-1914 gold standard and contributed to this regime’s credibility. “The credibility of the pre-war gold standard rested on international co-operation... Major crises were contained through overt, conscious co-operation among central banks and governments... The resources any one country could draw on when its gold parity was under attack far exceeded its own reserves; they included the resources of the other gold standard countries. This provided additional ammunition for defending their gold parity”. (Eichengreen, 1992, pp. 7-8). Eichengreen (1985) developed a similar view: “On occasion central banks and governments managed to achieve cooperative solutions to their problems, such as when they negotiated swap arrangements, earmarked gold, or extended international loans. Both central banks and governments clearly recognised their interdependence” (pp. 139-

140). In the same way, Cottrell (1982) noted that “Co-operation between Threadneedle Street and the *Rue des Petits Champs* was not a new development... By the early 1850s co-operation, at least of an intermittent form, was a well established practice. The two banks exchanged information and by 1854 telegraphed each other news of changes in their discount rates on a regular basis” (p. 132).

2. The thesis of non cooperation relies on three episodes only over the entire bimetallic period

Indeed, the controversy between the pros and the cons relies on a few episodes only. Most of the time, the arguments appear to be a pure matter of interpretation and the key point is that they refer to swap arrangements or international loans, not to discount rate coordination. According to Flandreau (1997, p. 740) “the period before 1854 seems to have been characterized by a number of successful international actions involving the Bank of France and the Bank of England”... “Early examples of central bank harmony included the 1825 London crisis... 1836, 1839¹..., 1846-1847” (p. 741)... “The last instance of cordial relations appears to have taken place in the spring of 1854... Hostilities started soon afterwards in August 1855”² (pp. 745-746). Flandreau took this example as proof of counter-productive and non cooperative equilibrium. He cited

¹ For instance, about the episode of 1839, Flandreau noted that Curtis in his final report praised d’Argout’s “influence and zealous activity that contributed to bring the matter in hand to a favourable consideration at the Bank of France” (p. 743). In Curtis Report, Bank of England archives, G4/62, cited by Flandreau, Curtis mentioned “a great desire on the part of the Bank of France to be able to establish a direct intercourse and interchange of good services between the establishment and the Bank of England... Such an arrangement might be of the highest advantage to the Bank of England... when it may be desirable to operate on the foreign exchanges ... such friendly and confidential relations between the two establishments would tend to produce when the situation of either Bank might require the aid and assistance of the other.”

² In august 1855, facing a decline in its reserve the Bank of France (p. 746) “asked a number of French Banks and bullion dealers to collect bills of immediate usance payable in London and send gold to Paris” without increasing its discount rate. The Bank of England reacted to this drain by raising its discount rate from 4.5% to 5% on 1 October and to 6% on 6 October. A message of Weguelin, the Governor of the Bank of England, to the French Governor followed (cited by Flandreau, p. 747), minimising the conflict and emphasising that “both past relations and current necessities impelled the two banks to ‘unite their strength’ rather than to fight”. “Weguelin concluded with a call for intensified exchange of information” (cited by Flandreau, p. 747). After a claim for help from the Bank of France, Weguelin refused to provide help, arguing that “the act of 1844 prevented the Bank of England from using its reserve to support foreign currencies” (cited by Flandreau, p. 748). According to Flandreau, p748, “the fight for gold appeared to be the only solution and the Bank of France replied in kind, raising its discount rate from 4 to 5% and subsequently to the 6% ceiling to meet the British policies”.

Bagehot's claim for an international lender of last resort as a supplementary illustration that co-operation between France and England did not exist³.

In fact, taking advantage of this episode to demonstrate the lack of co-operation between the two establishments is probably excessive. It could either be considered as a kind of day-to-day hostility: Viner (1937, p. 275), for instance, mentioned that "The manner in which the various commercial nations deal with the great mediums of exchange seems dictated by caprice rather than by any intelligent principle". Newmarch and Tooke (1857, VI, section 20) did not consider this episode as evidence of non cooperative attitude but as a mere precaution against an "*artificial withdrawing gold to the Bank of France*". This section 20 is entitled in an eloquent way '*System pursued by the Bank of France in 1855-56 for the purpose of procuring temporary artificial addition to its bullion reserve*'. The non cooperative argument appears to be questionable in this case: can this episode be compared to a failure of co-operation since the French demand did not obviously obey an imperative necessity? Cooperation does not necessarily mean systematic approval.

A second episode (October 1857) mentioned by Flandreau (1997) remains open to debate: "the Bank of France was certainly not ready to help London out, and in October 1857 the Bank of England had to suspend the act of 1844" (p. 750). Thus, a very strong assumption is made asserting that the suspension of the 1844 Act was caused by the French refusal to cooperate. "Relief was finally provided by the removal in France of the interest rate ceiling" (Flandreau, 1997, p. 750)... "It seems that the change in interest rate legislation in 1857 in France had certainly been in part motivated by the growing conflict with the Bank of England, thus forcing the French to give more leeway to their central bank" (p. 761). It has to be noted that this change in monetary policy was not limited to France. Other continental countries such as Belgium also modified their interest rate laws at the same time.

Diebolt and Parent (2008) gave evidence that using discount rate moves on the two sides of the channel revealed the will to benefit from a more useful and flexible regulatory tool.

Finally, Flandreau (1997, p. 752) mentioned a third evidence of non cooperative patterns: "The 1866 Overend Gurney panic was met with splendid indifference by the Bank of France, although the abundant liquidity of the Paris market at the time might have rendered cooperation feasible. Indeed, the Bank of France then enjoyed reserves at a record level ... This was certainly not cooperation". Does it mean it that the duty of the *Banque de France* would

³ "In the present cordial good understanding between France and England, it becomes the duty of both, to unit their strength in every way, not to divide it. I have often thought that an intimate correspondence upon emergencies between the two banks of France and England might be beneficial to both" (*Gold purchases*, p. 684).

have been to save a private financial British establishment even though the Bank of England did not ask for it?

To sum up, over the 1850-1870 period, the three episodes that Flandreau (1997) qualified as “Anglo-French disputes of the 1850s and 1860s” (p. 755) could easily be considered as mere occasional difficulties. This author described the “atmosphere of distrust in which these dealings occurred” (p. 751). Whatever the climate in the long run, these case studies do not concern directly the discount rate regulation but mainly swap arrangements. The point is that these dealings failed to become institutionalised and cooperation was not politically sealed: “This might have been partly related to the general political climate between the two countries, which was not overly favourable to such operations... parliaments generally resisted”... “opposition from the government certainly explains part of the secrecy” (Flandreau, 1997, p. 745). The difficulty to characterize the nature of the cooperation over the bimetallic period probably comes from the fact that swap arrangements or international loans were usually initiated by informal contacts. As underlined by Flandreau “interventions operate through the agency of one or several international bankers. This type of indirect arrangement could easily be understood since legal restrictions limited the ability of lending central banks” (Flandreau, 1997, p. 756). This author was correct when he noted that “the negotiations had also revealed that the Bank of France was a complex structure. Far from being a well-identified entity, with clear goals and objectives, it was a club where the (conflicting) interests of the banking elite were brokered” (p. 742). But the fact that these inter-central bank agreements were negotiated by private bankers members of the directory board (*conseil de régence*) of the *Banque de France* did not change anything at all: it was simply a form of co-operation dealt with by agents who were most familiar with international banking transactions⁴.

⁴ One can observe that during the bimetallic period, each time a monetary crisis occurred, whether in England or in the United-States, the calls for credit to the *Banque de France* recurred. The managers of the *haute banque*, specialised in international settlements and exchange bills acceptance formed the majority of the *Conseil de régence* and became the privileged go-between for these transactions. During periods of crisis, like in 1836, the *Conseil de régence de la Banque de France* allowed a loan to the *haute banque*, thus transferring a part of its metallic holding to sustain foreign central banks. This co-operation still in its early age may sometimes occur in a hostile environment. Viner (1937, p. 233) mentioned that in 1836 the Bank of England requested the help of the *Banque de France* “of course reluctantly”, and added that this necessity “was considered as particularly humiliating in Great-Britain” (we cannot obviously speak yet of *Entente cordiale* between the two countries!). For Thomas Tooke (cited by Kindleberger, 1994, p. 237, and extracted from *The Correspondance of Lord Overstone*), this loan is a “national humiliation”, “a cause of discredit”. Nevertheless, this bitterness did not impede the transaction...

As mentioned by Plessis (1998), “1839 is considered as the first important intervention on the international market: the transaction was dealt by Baring brothers; 14 Paris banks allowed a loan of 50 millions to the Bank of England, guaranteed by this bank, the signature of the Baring and by a deposit of public assets superior to the amount of the loan. Despite it

Obviously, we cannot talk about the bimetallic period as one of co-operation in the sense of multilateralism between institutions. However, definitely denying the existence of cooperation over the bimetallic period in the name of central bank fraternity⁵, that probably never existed over the world, at any time, is equally excessive. The “solidarity” over the bimetallic period was not limited to some sporadic swap arrangements between the *Banque de France* and the Bank of England. The problem is that when the argument of the discount rate coordination could be evoked it is systematically turned into an argument of rivalry.

3. Discount rate moves considered as rivalry and not coordination

The “solidarity” between the Bank of England and the *Banque de France* refers to a simultaneous increase of their respective domestic discount rates. Whether solidarity means rivalry between central banks for the sharing of gold and silver is the very heart of the debate. For instance, Asselain and Plessis (2003) argued that Bimetallism was not a coordinated system because the contacts between the Bank of England and the *Banque de France* were restricted and not very tight and that this practice was not continuous and official but relied on a kind of diplomacy of central banks limited to some “confidential trade of

was forbidden to the *Banque de France* to allow directly this loan, the *Conseil de régence* decided to accept to discount the bills drawn by the Barings on Paris banks and accepted by them. Among the *Conseil de régence* the great majority of Paris private financial institutions’ managers were present...”. If this kind of transaction cannot be precisely considered as a rescue of the Bank of England by the *Banque de France*, because the managers of Paris financial institutions directly co-operated with the Bank of England (just as the Rothschild did to help the Bank of the United States in 1839), it remains true that they did it with the agreement of the *Banque de France* (which accepted to discount the bills if needed), which is exactly the same.

In 1847, the *Banque de France* needed money to support its metallic holding. The Bank of England helped her with a temporary credit of 25 millions of *francs*, waiting for the *Banque de France* to obtain a similar amount from Baring brothers. As had been previously the case, the Baring advanced money to a *régent* of the *Banque de France* (Hottinguer) against French rent deposits. Still in 1847, French financial institutions played an important role when the *Banque de France* sold to the Saint Petersburg government for 50 millions of French rents against bills on Paris (Ramon, 1929, p. 206). Palmer, the Governor of the Bank of England justified in front of a parliamentary commission that it was better to agree directly with the main banks of the United-States, Hamburg, Amsterdam and Paris, rather than to export gold (cited by T. Joplin, p. 29).

⁵ As suggested by this author: “That the Bank of France performed essentially similar operations with both private and central banks shows that such dealings are appropriately described as those of merchants who find mutual benefits in exchanging assets, rather than as landmarks of international fraternity” (Flandreau, 1997, p. 752). But should cooperation necessarily mean central bank fraternity?

opinions and informations”. In the literature the analysis of cooperation through the channel of united action on discount rate by the *Banque de France* and the Bank of England is very peculiar: in no way is the issue of the efficiency of the discount rate regulation (for instance on the exchange rate) raised. Cooperation is seen as simple simultaneity of discount rate decisions and is associated with a non cooperative strategy: “It was not pure coincidence that the directory board (*Conseil de régence*) met *rue de la Vrillière* at the same time as the directors of the Bank of England did since they looked for reacting promptly to the decisions of the later and at adapting their behaviour immediately, if necessary” (Plessis, 1998, p. 116)... “The *Conseil de régence* did not hesitate to meet in extraordinary session once it had been informed by a telegraph from London; it did it without delay. As a matter of fact, British and French discount rates’ increases very often occurred the same day” (Plessis, 1998). The simultaneity of meetings written in the agenda of the *Banque de France* is considered here as a signal of hostility.

Does a concomitant increase of discount rates necessarily define a retaliatory measure against the adverse issuing institution? On the one side, Patterson (1867, pp. 2-6) denounced the “war between banks”. Mentioning the successive increases in the discount rates, he regretted that central banks “made a new kind of war, both civil and international, disastrous for the industry... in 1857 and 1864, the Bank of England went over to the offensive. The simple announcement that the Bank of England increased its discount rate run over Europe through the telegraph like an electric flame and each bank engaged the fight... The Bank of England increases its discount rate: it is the first step, the act of war... Immediately, the banks of other countries do the same”. In the famous *Enquête sur la circulation monétaire et financière*, this author wished for the end of “this system of rivalry and antagonisms” and called for a voluntary co-operation between issuing institutions. The follow-the-herd attitude of the *Banque de France* was denounced by Pereire: “The first concern of the *Banque de France* is the danger that an increase in the British discount rate represents for its metallic holdings”. They blamed the directors (*régents*) for “following servilely” the injunctions of the Bank of England and finally for their “docility” to import in France foreign monetary crises (cited by Plessis, 1998).

This thesis is still vivid. “The solidarity between banks meant in fact a hard competition for the sharing of the metallic stock” (Plessis, 1998). In this view, each issuing institution once facing a decrease in its own specie holdings is supposed to try to draw on other central banks’ metallic holdings. The Peel’s Act, which forbade the Bank of England to issue for more than 350 millions francs of notes uncovered by the equivalent in specie, encouraged the Bank of England to keep or get specie using discount rate increases. The historian of the *Banque de France* Plessis (1998) talks about “savage competition” and presents discount rates increases as a substitute means for specie purchases. Thus,

the *Banque de France* could easily “modify and take advantage of the effects of this international solidarity” (Plessis, 1998).

Obviously, this approach does not test its core proposition. We do not have any econometric test of the impact of the discount rate differential on the bimetallic stock holdings in France and England, nor do we have a measurement of the incidence of the discount rate differential on any outcome variable (such as the exchange rate; see for that Diebolt and Parent, 2008). Yet before drawing any definite conclusion, it would have been interesting to test the stabilizing properties of the discount rate differential on the bimetallic snake (Diebolt and Parent, 2008). More amazingly the notion of cooperation is defined without any reference to discount rate coordination (of which the discount rate differential is a proxy, see on that point Diebolt and Parent, 2008). This approach of the cooperation between central banks simply omits the channel of discount rate coordination. How could this view of non cooperation between central banks become so easily the cornerstone of conventional wisdom? In conclusion, we suggest an explanation.

Conclusion

Our reading is that the thesis of non cooperation between central banks is useful to the economic interpretation of Bimetallism as a self equilibrating system. Despite the extreme weakness of the historical arguments that we have discussed above (omission of cooperation as discount rate coordination, a hypothesis simply rejected and not tested; only two verified episodes of lending refusals between the British and French central banks over more than fifty years of Bimetallism), we consider that limiting the explorations of the influence of discount rate coordination on the Bimetallism stability has been a way of sealing the economic orthodox approach of Bimetallism. Indeed, the orthodox literature on Bimetallism insists on the self equilibrating role of bimetallic mechanisms. Velde and Weber (2000) showed that bimetalism was feasible, sustainable and stable. Oppers (2000) assessed the stabilizing effect of Bimetallism as being similar to that of an exchange rate target zone with bimetallic boundaries playing the role of reflecting barriers and the mint parity the part of absorbing barrier. By applying a monetary approach of the balance of payment Flandreau (1995, 1996, 2004) assumed that the double standard was an automatic system driven by market forces where the arbitrage between bills and specie markets kept the exchange rate back to the parity. In this tradition, the interest rate plays no role at all and discount rate coordination is not useful since the system is supposed to have self-equilibrating properties. In this article we have illustrated how using the historical context could distort the meaning of Bimetallism by sealing the academic view. Using history in a cliometric perspective (Diebolt and Parent, 2008) surely contrasts with the existing litera-

ture and delivers a revised story of bimetallism, certainly more in accordance with historical features.

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